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IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-394

MICHAEL PATERNO and PATERNO & SONS, INC.,

Petitioners,

against

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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The above named petitioners, Michael Paterno and Paterno & Sons, Inc., hereby respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit which affirmed judgments of the United States District Court for the Southern District of New York convicting petitioners and a co-defendant, George Denti, after trial before the court and a jury, on various counts under the indictment herein charging substantive violations of 26 U.S.C. §§ 7201 and 7206(1) and conspiracy to violate 26 U.S.C. § 7201. Petitioners' co-defendant is filing a separate petition for certiorari.

Opinion Below

The Court of Appeals rendered only a memorandum decision, which is not yet reported and which is printed in Appendix A, *infra*. No opinion was rendered by the District Court.

Jurisdiction

The judgment of the Court of Appeals was entered on July 18, 1974 (App. A, *infra*). A timely petition filed by petitioners for rehearing and for rehearing *in banc* was denied by the Court of Appeals on September 9, 1974 (App. B, *infra*). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

Constitutional Provisions, Statutes and Regulations Involved

The constitutional provisions, statutes and regulations here involved are the Fifth Amendment; 26 U.S.C. §§ 7201, 7206(1); 18 U.S.C. §§ 371, 2514, 6001, 6002, 6003; and Internal Revenue Practice General Procedural Rules § 601.107 (b)(2), as originally promulgated (1968), and as amended April 12, 1973. They are set forth in Appendix C, *infra*.

Questions Presented

1. (a) Whether the Federal immunity acts (18 U.S.C. §§ 2514, 6002, 6003) may properly be construed as authorizing a grant of immunity in a Federal criminal case only to a Government witness and not to a defense witness, even though the latter has previously testified as a Government witness at the same trial under a grant of immunity, and whether as so construed such statutes are violative of the guarantees of due process; and

(b) Whether it is error and a violation of due process for the trial court to deprive the defendant of the testimony of the defense witness in such a case by refusing to extend immunity to the witness with respect to such testimony, even though the witness's possible need of immunity has been suggested only by the prosecutor and the

trial court and only in connection with the prosecutor's anticipated cross-examination of the witness on the general issue of credibility.

2. Whether the appropriate sanction for the violation by the Internal Revenue Service of a regulation duly adopted and published by it, which provides that no charge of a violation of the tax laws shall be submitted to Regional Counsel for criminal prosecution without first giving the prospective defendant an opportunity to rebut the charge at an administrative conference, is to dismiss any indictment returned against the defendant in such a case without his having been given such an opportunity.

3. Whether an inference of consciousness of guilt may be drawn in a Federal criminal case from evidence of a false exculpatory statement made by the defendant, in the absence of any proof showing that he had knowledge of the falsity of such statement.

4. Whether it is error and a violation of due process for the trial court in a Federal criminal case to demean the defendant's defense in the presence of the jury and to erroneously hamper the presentation of such defense.

Statement of the Case

The indictment herein contained nine counts and charged a conspiracy to violate 26 U.S.C. § 7201, as well as substantive violations of 26 U.S.C. §§ 7201 and 7206, in relation to the corporate income tax returns of the corporate petitioner, Paterno & Sons, Inc. over a period of five fiscal years for the conspiracy charge and four fiscal years for the substantive charges, between 1965 and 1970 (9a-17a).*

* Unless otherwise specified, figures in parentheses followed by the letter "a" refer to the pages of defendants' joint Appendix in the Court of Appeals, and "G. Exh." refers to a Government Exhibit.

The corporate petitioner was engaged in the business of constructing and installing sewers. Its services on such projects included the necessary work of excavation and arranging for the carting away by trucks of the excavated earth, and for that purpose it hired truckers who supplied the trucks as well as the drivers. Petitioner Michael Paterno was the president and principal of the corporate petitioner. The co-defendant, George Denti, was the corporate petitioner's office manager and secretary-treasurer.

The indictment, in brief, charged that petitioners and co-defendant Denti had violated 26 U.S.C. §§ 7201 and 7206 by fraudulently deducting as business expenses in the corporate petitioner's income tax returns for the fiscal periods here involved, certain purported trucking expenses which had not been incurred. The expenses in question were the amounts represented by a total of 48 checks which had been issued by the corporate petitioner over a period of about four and one-half years to the order of five allegedly fictitious payees. All five payees purported to be truckers who had furnished trucks and trucking services to the corporate petitioner in connection with the carting away of earth excavated from various of its jobs. The checks had all been issued against invoices typed on printed letterheads which bore the names, addresses and telephone numbers of the respective payees. Most of the 48 checks had been signed by petitioner Paterno, but some had been signed by another corporate officer, Thomas Cohill (G. Exh.'s 1-48, 1a-12a, 14a-28a, 30a-34a, 36a-47a).

The Government made no effort to prove that the truck haulage work—for which the monies represented by the 48 checks in question were purportedly paid—was never performed. The Government further admitted that it had no knowledge or proof as to who received the monies represented by such checks (1827a, 1845a).

The Government, instead, merely adduced evidence to show that the names, addresses and telephone numbers of

the five payees were fictitious. The Government's proof thus showed that the five payees could not be located at the addresses or telephone numbers listed on the invoices submitted by them to the corporate petitioner, and that no record of such payees could be found in the files of governmental agencies such as the Internal Revenue Service, the Postal Service, the New York Department of Motor Vehicles, the New York Department of Taxation and Finance and the New York Workmen's Compensation Board, or of labor unions dealing with truckers.

There was also evidence which related solely to co-defendant Denti. The Government's proof thus showed that officers of the bank which cashed most of the 48 checks in question did so only after obtaining approval therefor by telephone from Denti (350a, 400a-402a); that the endorsements of the payees' names on five of the checks were in Denti's handwriting (840a, 842a-848a); and that Denti had given a statement to the Internal Revenue Service (hereinafter "IRS") indicating that one of the five payees, John Aurrichio, and possibly also another, Michael Catenzaro, had been hired through Taff Trucking, a firm which did trucking work for the corporate petitioner (1145a-1147a), whereas the owner of Traff Trucking, Salvatore Minichino, testified that he had never arranged for any trucker by the name of any of the five payees to work for Paterno & Sons, Inc. and did not know any such truckers (628a-630a).

On the other hand, there was not an iota of evidence to show that petitioner Paterno had ever arranged for the cashing of any of the checks in question or had ever authorized any bank officer or anyone else to cash any of them or that he had anything to do with the endorsements thereon, or that he had in any way received, or had any thing to do with, any of the proceeds thereof.

The evidence showed that the corporate petitioner used a great many truckers to cart away the excavated earth from its construction jobs. When James O'Reilly, one

of the corporate petitioner's construction superintendents, was asked, when testifying as a Government witness, whether he had maintained a list of truckers with whom his company did business during the period from 1965 to 1970, his answer was: "I didn't have a list of truckers. You know there's a thousand truckers" (1232a). When the company prepared for a particular job, the word would spread and numerous truckers would stop by to inquire as to when the actual excavation was to commence; they would be informed of the date, and they would then pass the word along to other truckers and friends (1285a-1286a). Many of the trucks used on those jobs did not even have truckers' names on them (639a).

It has consistently been petitioners' position that there was a complete absence of evidence to show that either petitioner Paterno or the corporate petitioner had any knowledge that any of the five payees in question were fictitious or non-existent or that either petitioner acted otherwise than in the good faith belief that the payees were the names of actual persons who were entitled to receive the checks in question for trucking equipment and services furnished to the corporate petitioner.

The only evidence offered by the Government to establish the essential elements of guilty knowledge, wilfulness and criminal intent on the part of petitioner Paterno—and through Paterno, on the part of the corporate petitioner—consisted of (1) the testimony of the company's job superintendent, O'Reilly, and its former bookkeeper, Mrs. Louise Ferraro, concerning certain statements made to them by petitioner Paterno relating to the five payees in question, which statements, the Government urged, warranted an inference of consciousness of guilt on Paterno's part, and (2) evidence which, the Government contended, showed that Paterno departed from his usual practice in paying the invoices of the five payees in question.

Petitioner Paterno's statements to O'Reilly and Mrs. Ferraro were made when the IRS first advanced the claim

in the course of its audit that the five payees were fictitious, and the statements amounted to nothing more than a denial of the IRS's claim in that regard. O'Reilly thus testified that what Paterno said to him was that "There are some trucks we said we had and they [the IRS] are saying we didn't have", or phrased differently, "They are questioning some trucks we claim we did have and they say we didn't have" (1260a-1262a). Mrs. Ferraro's testimony was that what Paterno told her was that whereas "they [the IRS] claimed that these truckers do not exist", "He said they did" (1112a). There was no evidence whatever to show that petitioner Paterno made the foregoing statements with knowledge of their falsity.

In support of its claim that Paterno departed from his usual practice in paying the invoices of the five payees in question, the Government relied primarily on the testimony of the corporate petitioner's two former bookkeepers, Mrs. Ferraro and her sister, Mrs. Anne Altro, who had prepared the checks for Paterno's signature. Mrs. Ferraro had worked for the company as a bookkeeper from 1964 to the spring of 1968, and Mrs. Altro had served as the company's bookkeeper from May 1968 through 1970 (1076a, 670a). They both testified that Paterno would never sign a check without substantiation to show that payment was due and owing (755a-757a, 1115a, 1123a). In the case of trucking expenses, the substantiation would generally consist either of delivery receipts or of entries in certain cost sheets relating to the particular job (1097a-1099a). Mrs. Ferraro testified that whenever she presented a check to Paterno for signature, she also presented back-up or substantiation material with it (1115a, 1123a), and there was no evidence to show that Paterno ever signed any check to any of the five payees in question during the period of Mrs. Ferraro's tenure without delivery receipts or entries in the cost sheets to substantiate the invoices being paid.

As regards the period of Mrs. Altro's tenure, she testified that whenever she presented a check to Paterno for

signature, there were always substantiating delivery tickets attached to the invoices (678a, 692a, 755a-757a). She also stated, however, that there were occasions when "George Denti would instruct her to prepare checks without delivery receipts" and would tell her "that he, George Denti, would explain the lack of substantiation to Mike Paterno" (685a-692a). On such occasions, according to her testimony, Denti would himself take the checks to Paterno for the latter's signature (692a). So far as her testimony showed, the practice about which she testified was not limited to invoices from the five payees in question.

There was no evidence to show what explanation Denti gave to Paterno on such occasions for the absence of delivery receipts, and there was no showing that Paterno ever signed a check on such occasions without there being some substantiation therefor, such as entries in the cost sheets.

Mrs. Ferraro testified that there were "hundreds of bills" which she would present for payment to Paterno at the end of each month (1092a-1097a). The evidence further showed that the company's expenses were very large; that the total expenses during the five-year period in question amounted to over 11 million dollars (G. Exh.'s 50-54); and that the equipment rental expenses during that period amounted to $882,808 (231a-236a; G. Exh. 173).

By way of defense, petitioners sought to prove that the corporate petitioner had, in fact, incurred the trucking expenses taken as deductions on its income tax returns, even though such expenses were represented by checks payable to truckers who might have used fictitious names in their billings for purposes of their own. Petitioner sought to establish that defense by expert testimony that the necessary work of hauling away the earth excavated from the corporate petitioner's construction jobs here involved, reasonably required the expenditures made there-

for by the corporate petitioner and deducted in its income tax returns, including the amounts represented by the checks to the payees in question. However, the trial court prejudicially demeaned that defense in the presence of the jury and made a number of erroneous rulings which thwarted the presentation of the defense.

At the close of the Government's case (1444a-1445a), and again at the close of the entire case (1680a-1683a), counsel for petitioners moved for judgments of acquittal, but the motions were denied. Neither petitioner Paterno nor co-defendant Denti took the stand.

Additional facts are set forth *infra*.

REASONS FOR GRANTING THE WRIT

1. The manner in which the Federal immunity statutes have been interpreted and applied by the courts below operates arbitrarily, in violation of the guarantees of due process, to deny the use of the mechanism of immunity to a defendant to secure the testimony of a recalcitrant witness, while making such mechanism available to the Government.

A novel and important question of general application is here presented, which drew the attention of Chief Justice Warren E. Burger, when he was sitting on the Court of Appeals for the District of Columbia, in *Earl* v. *United States*, 361 F.2d 531, 534, fn. 1 (D.C. Cir.). Justice Burger there expressed the view that it might well be a violation of due process if the Government were permitted to "use the immunity statute for its advantage" for the purpose of securing the testimony of a Government witness, and "the same mechanism" were not made "available to the accused" for the purpose of securing the testimony of a defense witness.

The arbitrariness of differentiating in that manner between the Government and the defendant is in fact highlighted in the present case, since here the witness sought to be called by petitioners had previously testified as a witness for the Government under a grant of immunity and petitioners were deprived of his testimony because they were unable to secure a grant of immunity for him as a defense witness. As a matter of fact, the testimony which petitioners sought to adduce from the witness would not have exposed him to any self-incrimination, and his possible need of immunity was suggested only by the prosecutor and the trial court and only in connection with the prosecutor's anticipated cross-examination of the witness on the general issue of credibility.

The witness here involved, James O'Reilly, had previously been granted immunity before the grand jury with respect to his grand jury testimony (1196a). Upon being called at the trial as a Government witness, he stated that he would testify without invoking his constitutional privilege (1198a), but the trial court advised that he should be granted immunity with respect to his trial testimony, and a separate order was accordingly made granting him such immunity (1201a-1203a).

O'Reilly then testified as a witness for the Government under such grant of immunity. On cross-examination, defense counsel attempted to elicit testimony from O'Reilly, and introduced certain documentary evidence through him, to serve as a foundation for subsequent expert testimony in support of the defense as to the costs incurred by the corporate petitioner for trucking expenses in hauling away excavated earth (1323a-1331a). After first flatly refusing to receive any evidence relating to that defense (1292a, 1294a, 1315a-1317a), the trial court ruled that it would permit petitioners to introduce such evidence through O'Reilly, but that they would have to call O'Reilly as their own witness on their case for that purpose (1331a).

When O'Reilly was thereafter called by petitioners as their witness, the trial court immediately interrupted to advise defense counsel and O'Reilly that the immunity with respect to his trial testimony, which he had been granted as a Government witness, would not extend to any testimony which he would be giving as a defense witness (1458a). Defense counsel advised the court that he proposed to limit the evidence which he planned to introduce through O'Reilly, essentially "to what can be called technical matters" such as "the plans, the photographs and the specifications" (1460a).

The prosecutor thereupon stated, in O'Reilly's presence, that "the questions that I hope to be asking him [O'Reilly] on cross examination may result in a decision to him that he may have committed some sort of criminal act, and I want him to be aware of that * * *" (1462a). The trial court added the comment, "Well, Mr. O'Reilly's history with us as a witness may invite that kind of approach * * *" (1462a).

Defense counsel then noted that O'Reilly had been permitted to give some preliminary testimony in support of the defense theory on cross examination; that the prosecutor had had a full opportunity to pursue the subject of O'Reilly's credibility on redirect examination; and that defendants would be deprived of a fair trial if the prosecutor were to be allowed "to take advantage of the inability of the defense to obtain a grant of immunity" for O'Reilly with respect to his testimony as a defense witness (1466a-1467a).

The trial court asked O'Reilly if he intended to invoke his privilege against self-incrimination, and O'Reilly stated that he did not and also said, "I was under the impression I was just going to be asked—", when he was interrupted by the trial court (1469a). The trial court then told O'Reilly, "Now whatever your impression is, you are subject to cross examination here", and further advised O'Reilly that "in that posture . . . [he] could

again plead . . . [his] privilege against self-incrimination, and nobody at that point could compel . . . [him] to answer" (1469a-1470a). Thereupon, O'Reilly stated, "Maybe I should have immunity again" (1470a), and he was excused by the trial court to seek independent legal advice (1471a). O'Reilly did not subsequently reappear as a witness.

It is submitted that petitioners were thereby erroneously deprived, in violation of due process, of their right to adduce essential testimony from the witness O'Reilly in support of their defense. It may be noted that one of the reasons thereafter given by the trial court for sustaining the Government's objections to certain hypothetical questions posed by defense counsel to petitioners' expert witness, Daniel J. O'Connell, with respect to the estimated costs involved in carting away excavated earth from various of the corporate petitioner's construction jobs, was that petitioners should have adduced testimony with respect to the underlying facts affecting such costs from "at least the job superintendent", i.e., O'Reilly (1570a-1571a).

The cases which have held that the trial court has no authority to grant immunity to a defense witness or to demand that the Government seek immunity for such a witness, have invariably involved situations where no immunity had been granted to a Government witness. See, e.g., *United States* v. *Berrigan*, 482 F.2d 171, 190 (3d Cir.); *United States* v. *Jenkins*, 470 F.2d 1061, 1063-4 (9th Cir.); *Cerda* v. *United States*, 488 F.2d 720, 723 (9th Cir.). In the factual setting of those cases, no advantage was conferred on the Government with respect to the availability of the mechanism of immunity, since the Government had neither sought nor obtained any grant of immunity for the purpose of securing the testimony of a recalcitrant Government witness.

In the present case, on the other hand, the Government had previously obtained a grant of immunity for the pur-

pose of securing the testimony of a Government witness—indeed the very same witness whom petitioners thereafter sought to call as a defense witness—and the effect of denying the use of the immunity statute to petitioners for the purpose of securing the testimony of that same witness as a defense witness was to place them at a decided disadvantage as compared with the Government. The considerations noted by Chief Justice Burger in *Earl* v. *United States, supra,* that it might well be a violation of due process to permit the Government to "use the immunity statute for its advantage" while denying the use of the statute to the defendant in the same case, are not only directly presented but have special pertinence in the present case. See also *United States* v. *Jenkins, supra,* 470 F.2d at 1064; *United States* v. *Jones,* 476 F.2d 885, 888 (D.C. Cir.) (Bazelon, Ch. J., dissenting).

In addition, the remarks addressed to O'Reilly by the prosecutor, as well as by the trial court, when O'Reilly was about to testify as a defense witness (1462a), fall squarely within the purview of the cases condemning statements by the trial court or the prosecutor which have an intimidating effect on a defense witness by calling the witness' attention to harmful consequences that might befall him if he testified for the defense. *Cf. Webb* v. *Texas,* 409 U.S. 95 (warning by the trial court to defense's sole witness that he could be convicted for perjury if he lied under oath); *United States* v. *Smith,* 478 F.2d 976 (D.C. Cir.) (warning by prosecutor to defense witness that he might incriminate himself and be subject to prosecution if he decided to testify for defense).

2. The courts below have, without warrant, absolved the Government from the binding force of its own regulations designed for the protection of taxpayers charged with violations of the tax laws.

Petitioners and co-defendant Denti filed a joint pre-trial motion in the District Court for dismissal of the indictment

on the ground that they had not been afforded any administrative conference, as required by Section 601.107(b)(2) of the Internal Revenue Practice General Procedure Rules, 33 F.R. 17235 (18a-19a, 22a-27a). Section 601.107(b)(2), which was promulgated in 1968 and duly published, provided as follows:

> "Every person who may be the subject of a recommendation for prosecution shall be given an opportunity to explain his participation in the alleged criminal violation prior to the submission of the case to Regional Counsel, unless compelling reasons exist to the contrary. At this interview the principal will be informed, by a general oral statement of the alleged fraudulent features of the case, to an extent consistent with protecting the Government's interests and, at the same time, making available to the taxpayer sufficient facts and figures to acquaint him with the nature, basis and other essential elements of the proposed criminal charge against him."

The Government did not deny that petitioners and Denti had not been granted any administrative conference, but asserted that where the IRS so decides, "there is no obligation to hold a conference on any level" (40a). The trial court denied said motion, without any discussion thereof in its memorandum decision (50a), and it also disregarded movants' alternative request for a hearing (19a). Though the issue was raised before the Court of Appeals, both on oral argument and in petition for rehearing, that court did not write an opinion thereon.

The IRS investigation in this case commenced about December 1970 (198a). On the argument of the appeal herein before the Court of Appeals, Government counsel stated that the IRS had submitted the case to Regional Counsel no later than April 11, 1973. The indictment herein was filed on May 3, 1973 (1a).

Section 601.107(b)(2) was amended by a duly published revised regulation which recited that it was to become effective on April 12, 1973. The revised regulation deleted the mandatory language of the section requiring that the taxpayer *"shall be given* an opportunity to explain his participation in the alleged criminal violation", and provided in place thereof that an administrative conference was to be made available only if the taxpayer requested it, or the Chief of the Intelligence Division determined that it would be in the Government's best interests. The revised regulation reads as follows (38 F.R. 9227):

> "A taxpayer who may be the subject of a criminal recommendation will be afforded a district intelligence conference when he requests one or where the chief, Intelligence Division, makes a determination that such a conference will be in the best interests of the Government. At the conference, the IRS representative will inform the taxpayer by a general oral statement of the alleged fraudulent features of the case, to the extent consistent with protecting the Government's interests, and, at the same time, making available to the taxpayer sufficient facts and figures to acquaint him with the basis, nature, and other essential elements of the proposed criminal charges against him."

Though, as noted, the effective date of the revised regulation was specified in its published form as April 12, 1973, the Government contended in the courts below that the change in regulation actually took effect about four months prior thereto, on December 14, 1972, when an internal and unpublished memorandum from the Assistant Commissioner (Compliance) and the Chief Counsel of the IRS was circulated to all Regional Commissioners and Regional Counsel in the IRS, announcing their decision "to eliminate the requirement" for an administrative conference and directing that such a conference would thereafter be held

only if the taxpayer requested it or the Chief of the Intelligence Division believed it to be in the best interest of the IRS. However, as the Government admitted in its brief in the Court of Appeals, "the publicly available version of this IRS regulation" was not "amended to reflect the change" until April 12, 1973. It is clear that until the latter date, when the revised regulation was first published in the Federal Register, as was the original regulation which it purported to amend, the revised regulation was "simply a housekeeping provision of the Department" which was not entitled to any legal effect. See *Sullivan* v. *United States*, 348 U.S. 170, 173.

Thus, when the IRS submitted petitioners' case to Regional Counsel for criminal prosecution without having given petitioners any opportunity for an administrative conference, it violated its own regulations in effect at that time. Such regulations had the force and effect of law and were binding on the Government until they were amended or revoked. *United States ex rel. Accardi* v. *Shaughnessy*, 347 U.S. 260, 265; *United States* v. *Nixon*, 41 L. Ed. 2d 1039, 1057.

Under the regulations in effect when this case was submitted for criminal prosecution to Regional Counsel, unlike the revised regulations which thereafter took effect on April 12, 1973, there was no requirement that the prospective defendant make a request for an administrative conference. On the contrary, Section 601.107(b)(2) made it mandatory that the prospective defendant "*shall be given* the opportunity to explain his participation in the alleged criminal violation prior to the submission of the case to Regional Counsel", with the only exception provided for being where "compelling reasons exist to the contrary". The Government has never advanced any claim of such "compelling reasons" in this case.

It is thus immaterial that no formal request for a conference was ever made by petitioners. Indeed, any such re-

quest would have been a sheer futility since Government counsel conceded on the argument before the Court of Appeals that the IRS had made a decision not to grant any conference to petitioners and Denti even if they requested one.

By reason of the Government's arbitrary and unjustifiable violation of its own published regulations, petitioners were here denied the opportunity to persuade the IRS not to proceed with any criminal prosecution. Petitioners were thereby deprived of a substantial right, since the case against Paterno on the issues of guilty knowledge and criminal intent was extremely tenuous. Furthermore, the technical rules of evidence which hampered petitioners' attempt to prove their defense at the trial through expert testimony, would not have been controlling at an administrative conference.

It is submitted that the appropriate sanction in such a case, on the analogy of decisions in other comparable situations, is to invalidate the criminal prosecution, the initiation of which violated petitioners' rights, by dismissing the indictment herein. *Cf. Yellin* v. *United States,* 374 U.S. 109, 121-123; *Service* v. *Dulles,* 354 U.S. 363; *Vitarelli* v. *Seaton,* 359 U.S. 535.

3. By upholding the conviction of petitioner Paterno herein, the courts below have in effect dispensed with the essential elements of wilfulness and guilty knowledge in a Federal criminal tax prosecution.

It is settled that a defendant charged with having violated 26 U.S.C. § 7201 must be shown to have "acted wilfully and knowingly with the specific intent to evade the tax." *United States* v. *Coblentz,* 453 F.2d 503, 505 (2d Cir.), cert. den. 406 U.S. 917; *Spies* v. *United States,* 317 U.S. 492, 497-9. Wilfulness and guilty knowledge are also essential elements of the crimes of conspiracy to violate 26 U.S.C.

§ 7201 (*Ingram* v. *United States,* 360 U.S. 672, 678), and of the crime defined by 26 U.S.C. § 7206 (*United States* v. *Bishop,* 412 U.S. 346).

Assuming, *arguendo,* that the Government's proof was sufficient, *prima facie,* to show that the names of the five payees in question were not those of actual persons or firms, there was a complete absence of evidence to show that either petitioner Paterno or the corporate petitioner had any knowledge that any of such payees were fictitious or non-existent, or that either of such petitioners acted otherwise than in good faith in signing the checks here involved. Though there might have been sufficient evidence to show guilty knowledge on Denti's part, there was no basis whatever for imputing Denti's knowledge or intent to petitioner Paterno.

One of the major props on which the Government sought to predicate its case against petitioner Paterno was the evidence of the false exculpatory statements made by him to O'Reilly and Mrs. Ferraro. The general rule is that "exculpatory statements, when shown to be false, are circumstantial evidence of guilty consciousness and have independent probative force." See *United States* v. *Lacey,* 459 F.2d 86, 89 (2d Cir.). That rule, however, is subject to the qualification that the person making the false exculpatory statement must be shown to have made it wilfully and "with knowledge of the falsity". See *Rizzo* v. *United States,* 304 F.2d 810, 830 (8th Cir.); *cf. Ashcraft* v. *Tennessee,* 327 U.S. 274, 278.

Manifestly, there would be no basis or warrant for drawing an inference of a defendant's consciousness of guilt by reason of his having made a false exculpatory statement, unless he was shown to have had knowledge of its falsity. The very concept of consciousness of guilt necessarily implies a mental state in which the actor is fully conscious of the fact that he is making a false state-

ment, and it has no place where the person making the statement in good faith believes that it is true.

Thus, in the cases in which probative force has been accorded to a false exculpatory statement, the statement has invariably related to facts the truth or falsity of which is necessarily personally known to the defendant, so that proof of the falsity of the statement also establishes the defendant's knowledge of such falsity; as in the case of false statements relating to the defendant's residence, employment or associations, or his activities at or near the scene of the crime. E.g., *United States* v. *Smolin,* 182 F.2d 782, 786 (2d Cir.); *United States* v. *Wilson,* 342 F.2d 43, 44-5 (2d Cir.); *United States* v. *Trudo,* 449 F.2d 649, 651 (2d Cir.); *United States* v. *Kirkpatrick,* 458 F.2d 864, 867 (7th Cir.); *United States* v. *Massarotti,* 462 F.2d 1328, 1330 (2d Cir.).

In the present case, on the other hand, the question whether the five payees were existent or non-existent was not a matter of which petitioner Paterno necessarily had personal knowledge. Indeed, the burden was on the Government to establish, among other elements, not only that the five payees were non-existent, but that petitioner Paterno had knowledge thereof when he signed the checks to such payees and thereafter signed the corporate income tax returns. To allow an inference of consciousness of guilt on Paterno's part—and on the basis thereof, a further inference of guilty knowledge on his part—to be drawn, as was here done, merely because of statements made by Paterno in which he disputed the Government's claim as to the non-existence of the five payees, without any showing that Paterno had knowledge of the falsity of such statements, is equivalent to allowing the Government to obtain a conviction of Paterno without actually proving the essential elements of wilfulness and guilty knowledge on his part.

Furthermore, there is cogent authority that evidence of a false exculpatory statement on a defendant's part is not

sufficient of itself to warrant conviction. *United States* v. *McConney,* 329 F.2d 467, 470 (2d Cir.); see *United States* v. *Lacey,* 459 F.2d 86, 89-90 (2d Cir.). Cf. also *Wong Sun* v. *United States,* 371 U.S. 471, 483, fn. 10, involving the analogous situation of proof of flight.

Nor was any of the Government's other evidence legally sufficient to show wilfulness or guilty knowledge on Paterno's part. The Government's claim was that whereas Paterno's general practice was to insist, before signing any checks, that the particular invoices be supported by substantiating material, he did not follow that practice in the case of the checks to the order of the five payees in question. There was, however, a complete failure of proof by the Government on that score.

As respects the period of Mrs. Ferraro's tenure—from 1964 to May 1968, she testified that whenever she presented a check to Paterno for signature, she also presented back-up or substantiation material with it, and there was not the slightest suggestion in her testimony that Paterno departed from that practice in the case of the checks to the five payees in question (see *supra,* p. 7).

As regards the tenure of Mrs. Altro—from May 1968 through 1970, Mrs. Altro did state that there were occasions when co-defendant Denti would "instruct her to prepare checks without delivery receipts" and would tell her that he "would explain the lack of substantiation" to Paterno, and that on such occasions Denti would himself take the checks to Paterno for the latter's signature (see *supra,* p. 8). There was, however, no evidence to show what explanation Denti gave to Paterno on such occasions for the absence of delivery receipts, and there was no showing that Paterno ever signed a check on such occasions without there being some substantiation therefor, such as entries in the cost sheets.

Denti could obviously have given Paterno some reasonable explanation for the unavailability of delivery receipts

on those particular occasions, and to attempt to draw an inference of guilty knowledge on Paterno's part by speculating as to what Denti might have told him, would amount to an impermissible resort to suspicion instead of proof. *Cf., United States* v. *Cirillo,* —— F.2d —— (2d Cir.), decided May 7, 1974; *United States* v. *Jensen,* 462 F.2d 763, 765 (8th Cir., per Mr. Justice Tom Clark); *United States* v. *Barnes,* 383 F.2d 287, 291 (6th Cir.). Furthermore, even negligence on Paterno's part in permitting himself to be deceived by Denti, would not be sufficient to establish that Paterno himself had acted with the requisite wilfulness, guilty knowledge and criminal intent. See *Standard Oil Company of Texas* v. *United States,* 307 F.2d 120, 130 (5th Cir.).

4. The trial court deprived petitioners of a fair trial by demeaning their defense in the presence of the jury and hampering their presentation thereof.

As shown above, by way of defense, petitioners sought to prove that regardless of whether the payees in question used fictitious names in their billings for purposes of their own, the monies represented by the checks payable to such payees had actually been expended by the corporate defendant for the necessary work of hauling away excavated earth from the job sites involved. The facts sought to be established by that defense would also have confirmed that Paterno had acted in good faith, and not wilfully or with guilty knowledge, in signing the checks to the five payees in question for excavation hauling expenses.

In his charge to the jury, the trial judge submitted the foregoing defense to the jury, taking note of petitioners' claim that the amounts represented by the checks to the five payees in question "were in fact paid for required trucking services rendered" to the corporate petitioner (1902a-1903a). However, the trial judge had previously, in the course of the trial, irrevocably prejudiced the presentation of the defense by stating on several occasions

in the presence of the jury that the basic issue in the case was "whether these five truckers, or any of them, were existent or non-existent" (1315a-1316a, 1616a).

In addition, the trial judge prejudicially hampered the presentation of the defense by various exclusionary rulings grounded on the position that any evidence along the lines of such defense which did not meet the issue as to the existence of the five payees would be excluded as irrelevant (1293a-1294a, 1307a-1308a, 1315a-1317a). Further, when defense counsel stated that he planned to have an expert testify as to the cost entailed in hauling away the earth excavated from the corporate petitioner's various job sites, the trial judge stated—though not in the presence of the jury—that he would send the matter *"to a grand jury to be studied"*, and he described the defense as one "border[ing] on fantasies" (1324a-1325a; emphasis supplied).

Petitioners' expert witness, O'Connell, was a consulting engineer and former associate professor at Manhattan College School of Engineering (1505a-1509a). By examining the specifications for three of the five jobs on which the trucking expenses of the corporate petitioner had been incurred, O'Connell was able to estimate the specific quantities of excavated earth carted away on each of the three jobs (1509a-1511a, 1519a-1520a, 1549a, 1632a). He was also permitted to testify as to the size of the dump trucks used during the period involved, and the cost per day of renting a truck with a driver during that period, as reflected by various invoices in evidence (1518a, 1519a, 1621a-1622a) The only other element to be considered in calculating the costs involved consisted of the number of trips each truck could reasonably make per day between the job site and the dump site, and that depended on the mileage and the time required for each round trip (1568a-1569a).

It s submitted that O'Connell was fully qualified to give his expert opinion as to the foregoing matters. The trial

court, however, repeatedly refused to allow O'Connell to do so (1550a-1554a, 1564a-1575a, 1576a-1589a, 1613a-1614a, 1622a-1623a), and stated that the questions which were put to O'Connell by defense counsel were objectionable because they called for "estimates" rather than "actualities" as to the "amount of trucking" (1574a-1575a). It is submitted, however, that where, as here, proof of "actualities" was not readily available, it was error for the court to refuse to receive competent expert testimony of soundly based "estimates". *Cf., Gilbert* v. *Gulf Oil Corp.*, 175 F.2d 705, 709 (4th Cir.).

The trial court further stated that petitioners should have adduced the testimony of "at least the job superintendent"—i.e., O'Reilly—with respect to the underlying facts, to serve as a predicate for O'Connell's expert testimony (1570a-1571a). Yet, as shown above, petitioners were deprived of O'Reilly's testimony by reason of the action of the prosecutor and the trial court in confronting O'Reilly with the risk of self-incrimination, and the trial court's refusal to extend immunity to O'Reilly with respect to his testimony as a defense witness (*supra,* pp. 11-12).

CONCLUSION

For the reasons set forth above, this petition for a writ of certiorari should be granted.

Respectfully submitted,

ARTHUR KARGER,
Counsel for Petitioners
600 Madison Avenue
New York, New York 10022.

APPENDIX A

Decision and Opinion of the United States Court of Appeals for the Second Circuit.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 18th day of July one thousand nine hundred and seventy-four.

Present:

WILLIAM HUGHES MULLIGAN, U.S.C.J.
HARRISON L. WINTER, U.S.C.J.
JON O. NEWMAN, U.S.D.J.
Circuit Judges.

74—1554
74—1555
74—1556

United States of America,

Plaintiff-Appellee,

v.

Michael Paterno, George Denti and Paterno and Sons, Inc.,

Defendants,

Michael Paterno, Paterno & Sons, Inc., George Denti,

Defendants-Appellants.

Appeal from the United States District Court
for the Southern District of New York.

Appendix A

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged and decreed that the judgments of conviction of said District Court be and they hereby are affirmed. During argument of the appeal the Government made a comparison between the average costs for engaging recognized truckers and those claimed to be fictitious. Counsel for Paterno moved orally after argument to submit responding papers. In view of the overwhelming evidence of guilt we do not consider the point material. The motion is denied.

William Hughes Mulligan, U.S.C.J.
Harrison L. Winter, U.S.C.J.
Jon O. Newman, U.S.D.J.

APPENDIX B

Order of Court of Appeals Denying Petition for Rehearing.

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

Docket No. 74-1554

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the ninth day of September, one thousand nine hundred and seventy-four.

Present: HON. HARRISON L. WINTER,
HON. WILLIAM H. MULLIGAN,
Circuit Judges.
HON. JON O. NEWMAN,
District Judge.

UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

MICHAEL PATERNO, GEORGE DENTI and PATERNO AND SONS, INC.,

Defendants-Appellants.

A petition for a rehearing having been filed herein by counsel for the appellant, Michael Paterno and Paterno and Sons, Inc.,

Upon consideration thereof, it is

Ordered that said petition be and hereby is denied.

A. DANIEL FUSARO
Clerk

Appendix B

Order of Court of Appeals Denying Petition for Rehearing In Banc.

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

Docket No. 74-1554

At a stated term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the ninth day of September, one thousand nine hundred and seventy-four.

UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

MICHAEL PATERNO, PATERNO AND SONS, INC., GEORGE DENTI,

Defendants-Appellants.

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the appellant, Michael Paterno, Paterno and Sons, Inc., and no active judge or judge who was a member of the panel having requested that a vote be taken on said suggestion,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is DENIED.

IRVING R. KAUFMAN
Chief Judge

APPENDIX C

Constitutional Provisions, Statutes and Regulations Involved

U.S. Const., Amend. V

No person shall be held to answer for a captial, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

18 U.S.C. § 371. Conspiracy to commit offense or to defraud United States

If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both.

If, however, the offense, the commission of which is the object of the conspiracy, is a misdemeanor only, the punishment for such conspiracy shall not exceed the maximum punishment provided for such misdemeanor.

26 U.S.C. § 7201. Attempt to evade or defeat tax

Any person who wilfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided

by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $10,000, or imprisoned not more than 5 years, or both, together with the costs of prosecution.

26 U.S.C. § 7206. Fraud and false statements

Any person who—

> (1) Declaration under penalties of perjury—Willfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter; • • •

shall be guilty of a felony and, upon conviction thereof, shall be fined not more than $5,000, or imprisoned not more than 3 years, or both, together with the costs of prosecution.

18 U.S.C. § 2514. Immunity of witnesses

Whenever in the judgment of a United States attorney the testimony of any witness, or the production of books, papers, or other evidence by any witness, in any case or proceeding before any grand jury or court of the United States involving any violation of this chapter or any of the offenses enumerated in section 2516, or any conspiracy to violate this chapter or any of the offenses enumerated in section 2516 is necessary to the public interest, such United States attorney, upon the approval of the Attorney General, shall make application to the court that the witness shall be instructed to testify or produce evidence subject to the provisions of this section, and upon order of the court such witness shall not be excused from testifying or from producing books, papers, or other evidence on the ground that the testimony or evidence required of him may

tend to incriminate him or subject him to a penalty or forfeiture. No such witness shall be prosecuted or subjected to any penalty or forfeiture for or on account of any transaction, matter or thing concerning which he is compelled, after having claimed his privilege against self-incrimination, to testify or produce evidence, nor shall testimony so compelled be used as evidence in any criminal proceeding (except in a proceeding described in the next sentence) against him in any court. No witness shall be exempt under this section from prosecution for perjury or contempt committed while giving testimony or producing evidence under compulsion as provided in this section.

18 U.S.C. § 6001. Definitions

As used in this part—

(1) "agency of the United States" means any executive department as defined in section 101 of title 5, United States Code, a military department as defined in section 102 of title 5, United States Code, the Atomic Energy Commission, the China Trade Act registrar appointed under 53 Stat. 1432 (15 U.S.C. sec. 143), the Civil Aeronautics Board, the Federal Communications Commission, the Federal Deposit Insurance Corporation, the Federal Maritime Commission, the Federal Power Commission, the Federal Trade Commission, the Interstate Commerce Commission, the National Labor Relations Board, the National Transportation Safety Board, the Railroad Retirement Board, an arbitration board established under 48 Stat. 1193 (45 U.S.C. sec. 157), the Securities and Exchange Commission, the Subversive Activities Control Board, or a board established under 49 Stat. 31 (15 U.S.C. sec. 715d);

(2) "other information" includes any book, paper, document, record, recording or other material;

(3) "proceeding before an agency of the United States" means any proceeding before such an agency with respect to which it is authorized to issue subpenas and to take testimony or receive other information from witnesses under oath; and

(4) "court of the United States" means any of the following courts: the Supreme Court of the United States, a United States court of appeals, a United States district court established under chapter 5, title 28, United States Code, the District of Columbia Court of Appeals, the Superior Court of the District of Columbia, the District Court of Guam, the District Court of the Virgin Islands, the United States Court of Claims, the United States Court of Customs and Patent Appeals, the Tax Court of the United States, the Customs Court, and the Court of Military Appeals.

18 U.S.C. § 6002. Immunity generally

Whenever a witness refuses, on the basis of his privilege against self-incrimination, to testify or provide other information in a proceeding before or ancillary to—

(1) a court or grand jury of the United States,

(2) an agency of the United States, or

(3) either House of Congress, a joint committee of the two Houses, or a committee or a subcommittee of either House,

and the person presiding over the proceeding communicates to the witness an order issued under this part, the witness may not refuse to comply with the order on the basis of his privilege against self-incrimination; but no

testimony or other information compelled under the order (or any information directly or indirectly derived from such testimony or other information) may be used against the witness in any criminal case, except a prosecution for perjury, giving a false statement, or otherwise failing to comply with the order.

18 U.S.C. § 6003. Court and grand jury proceedings

(a) In the case of any individual who has been or may be called to testify or provide other information at any proceeding before or ancillary to a court of the United States or a grand jury of the United States, the United States district court for the judicial district in which the proceeding is or may be held shall issue, in accordance with subsection (b) of this section, upon the request of the United States attorney for such district, an order requiring such individual to give testimony or provide other information which he refuses to give or provide on the basis of his privilege against self-incrimination, such order to become effective as provided in section 6002 of this part.

(b) A United States attorney may, with the approval of the Attorney General, the Deputy Attorney General, or any designated Assistant Attorney General, request an order under subsection (a) of this section when in his judgment—

(1) the testimony or other information from such individual may be necessary to the public interest; and

(2) such individual has refused or is likely to refuse to testify or provide other information on the basis of his privilege against self-incrimination.

***Internal Revenue Practice General Procedure Rules*, § 601.107(b)(2), added Nov. 21, 1968, 33 F.R. 17235:**

§ 601.107. Intelligence functions.

• • •

(b) Investigative procedure. • • •

(2) Every person who may be the subject of a recommendation for prosecution shall be given an opportunity to explain his participation in the alleged criminal violation prior to the submission of the case to Regional Counsel, unless compelling reasons exist to the contrary. At this interview the principal will be informed, by a general oral statement of the alleged fraudulent features of the case, to an extent consistent with protecting the Government's interests and, at the same time, making available to the taxpayer sufficient facts and figures to acquaint him with the nature, basis and other essential elements of the proposed criminal charge against him. • • •

***Internal Revenue Practice General Procedure Rules*, § 601.107(b)(2), amended April 12, 1973, 38 F.R. 9227:**

§ 601.107. Intelligence functions.

• • •

(b) Investigative procedure. • • •

(2) A taxpayer who may be the subject of a criminal recommendation will be afforded a district intelligence conference when he requests one or where the Chief, Intelligence Division, makes a determination that such a conference will be in the best interests of the Government. At the conference, the IRS representative will inform the taxpayer by a general oral statement of the alleged fraudulent features of the case, to the extent consistent with protecting the Government's interests, and, at the same time, making available to the taxpayer sufficient facts and figures to acquaint him with the basis, nature, and other essential elements of the proposed criminal charges against him.

In the Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-394

MICHAEL PATERNO AND PATERNO & SONS, INC., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The district court did not render a written opinion. The *per curiam* opinion of the court of appeals (Pet. App. A) is reported at 498 F.2d 1396.

JURISDICTION

The judgment of the court of appeals was entered on July 18, 1974. Petitions for rehearing and for rehearing *en banc* were denied on September 9, 1974 (Pet. App. B). The petition for a writ of certiorari was filed on October 8, 1974. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the evidence was sufficient to support the verdict against petitioner Michael Paterno.

2. Whether petitioners were improperly deprived of the testimony of a witness who had testified for the prosecution under a grant of immunity where the defense requested that he be excused and recalled pursuant to subpoena, at which time the court stated it would make a decision on immunity when the witness returned but the witness never returned.

3. Whether petitioners' indictment was invalid because they were not given a formal opportunity to present their defense to the Internal Revenue Service before the case was referred to the Office of Regional Counsel.

4. Whether the district court demeaned petitioners' defense in the presence of the jury and improperly excluded the testimony of an expert witness.

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED

The relevant constitutional provisions, statutes and regulations are set forth at Pet. App. C.

STATEMENT

After a jury trial in the United States District Court for the Southern District of New York, petitioners and George Denti[1] were convicted on all counts of a nine-count indictment charging various violations of the income tax laws. The first count charged Michael Paterno, George Denti and Paterno & Sons, Inc., with conspiring to evade the income taxes of the corporation for each of its fiscal years from 1966

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[1]George Denti has filed a separate petition for a writ of certiorari (No. 74-406). Because his contentions parallel those in the petition in this case, we are serving upon his counsel a copy of this brief in opposition.

through 1970, in violation of 18 U.S.C. 371. Counts two through five charged the individuals and the corporation with attempting to evade the corporation's income taxes from 1967 through 1970, in violation of 26 U.S.C. 7201. Counts six through nine charged Paterno and Denti with subscribing the false income tax returns of the corporation for the same fiscal years, in violation of 26 U.S.C. 7206 (1). Petitioner Michael Paterno was sentenced to concurrent terms of nine months' imprisonment on each count and fined $20,000. The corporation was fined $25,000.

The government's proof established that over a four-year period Paterno & Sons, Inc., a large sewer constructing company which derived its income principally from contracts with New York City and other municipalities, issued more than $145,000 in checks that were fraudulently claimed as trucking expenses on its income tax returns. The names on the checks as payees, and on invoices purporting to show trucking services rendered to the corporation, were fictitious. These fraudulent deductions reduced the corporation's reported tax liability by almost $75,000 (App. 1079a-1082a, 1148a-1195a, 1201a, 1361a-1417a).[2]

During the four years in question, Michael Paterno was the corporation's president and sole stockholder, and George Denti was its secretary-treasurer and office manager (App. 623a, 1079a-1084a; Govt. Exs. 99-104). A certified public accountant prepared the corporation's income tax returns from the corporate records, which showed truck rental expenses of approximately $320,000 over the four-year period (App. 139a-150a). Almost half of those alleged expenses had been paid by means of a total of 48 checks to five named persons, and the corporate records included documents purporting to be invoices from those five payees for work performed in supplying trucks and trucking services in connection with hauling earth from excavation projects at five different job sites.

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[2]"App." refers to the joint appendix filed in the court of appeals.

The addresses and telephone numbers on those invoices were fictitious (App. 210a-215a, 364a-392a; Govt. Ex. 79). Of the 48 checks which totalled $148,297.82, 39 had been cashed at the corporation's own bank, the Royal National Bank, and nine had been cashed at a bar (Govt. Exs. 1-48). While the bank's procedures required a bank officer to obtain identification from a payee before permitting a check in excess of $100 to be cashed, this policy was not followed with regard to the 39 checks. Instead, Denti telephoned the bank official in charge and authorized him to cash the checks (App. 343a-353a, 397a-400a). These 39 checks were the only checks of the corporation ever to be cashed in this manner (App. 355a, 403a, 563a). The owner of a bar and grill in Manhattan testified that he had cashed the nine remaining checks but was unable to recall the identity of the payees (App. 599a-606a; Govt. Exs. 24, 26, 36, 38, 39, 41-43, 45). Finally, James O'Reilly, who was employed by the corporation as a superintendent, testified under a grant of immunity that he had never heard of the five alleged truckers who were named as payees on the checks (App. 1238a, 1243a).

Daniel J. O'Connell, a civil engineer, was called by the defense to estimate the amount of earth that had to be removed from the various sites, the number of truckloads that would be needed for such work, and the cost of such a movement of earth. Because of the variables involved and the inherent unreliability of this type of analysis on the facts in this case, the court did not permit testimony as to estimates of the total cost of moving the earth (App. 1580a-1587a, 1609a-1614a).

ARGUMENT

1. Petitioners contend (Pet. 17-21) that there was no evidence that they knew that the payees were fictitious persons. But as the foregoing description of the evidence demonstrates, there was ample proof that Paterno had knowledge of, and took an active part in, the income tax fraud of his corporation. He was the president and sole owner of the corporation, and was in complete charge of its operations. He prepared the bids and estimates submitted by the corporation for its jobs, negotiated directly with the contractors for the corporation and the municipalities that contracted with the corporation, and spent a good portion of each day inspecting the sites of the jobs. He was also in complete charge of the fiscal affairs of the corporation and signed almost all of its expense checks (App. 1079a-1082a, 1090a-1094a, 1210a; Govt. Exs. 14-48).

The evidence firmly established that Paterno controlled the corporation's payment of bills. From a monthly list of outstanding bills, he determined those that would be paid (App. 691a-692a, 1090a-1094a). He would never sign a check in payment of a bill unless he had examined the invoice and substantiated the amount on the invoice (App. 756a, 1031a-1034a, 1123a). In the case of trucking services, which were the alleged basis for the issuance of the 48 checks in question to the five fictitious payees, the required substantiation was normally a delivery receipt. Such a receipt was prepared on a daily basis by the trucker for each truck he was supplying to the corporation and signed by an employee of the corporation at the job site to confirm the truck's presence (App. 1214a-1217a). However, no

delivery receipts from any of the five fictitious payees were ever introduced into evidence at trial, nor were any provided to the government in response to its subpoena.[3] Moreover, the payments to the five fictitious payees for trucking services were substantial, exceeding the payments made to the large number of legitimate truckers (Govt. Ex. 173). In fact, the largest single payment in each year for trucking expenses went to a fictitious payee (App. 714a-715a, 1093a-1096a). This evidence provided ample basis for an inference that Paterno, and through him, the corporation, knew that the payees of the 48 checks were fictitious persons who had not in fact performed any services for the corporation.

There was also testimony to the effect that although Denti and Paterno insisted at various times and to various individuals that the five payees were legitimate truckers (App. 357a-358a, 406a-409a, 1112a-1113a, 1135a-1137a, 1266a-1269a), they both later denied that they had ever heard of the payees (App. 544a-546a, 628a-630a, 1269a). Petitioners argue (Pet. 18-19) that Paterno's false exculpatory statements concerning the identities of the five payees were improperly admitted because the government allegedly failed to show that Paterno knew his statements to be false. But as we have shown above, there was sufficient other evidence from which the jury could reasonably conclude that Paterno knew the payees were fictitious.

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[3]In addition, one of the corporation's bookkeepers testified that a delivery receipt was almost always stapled to the invoice and that without such a delivery receipt Paterno would not approve the payments or sign the checks. Thus, there was a staple mark in every one of the invoices from legitimate truckers in evidence at the trial, while such a staple mark was not present on over 80 percent of the invoices for the fictitious payees (App. 779a, 783a). Since the delivery receipts from the five payees were never produced despite subpoena and court order, this evidence of the absence of staple marks on the invoices from the five payees allowed the jury to infer that they never existed and that Paterno was not following his own practice in paying trucking expenses but rather was making payments for unknown reasons.

2. Petitioners further contend (Pet. 9-13) that the defense was improperly deprived of the testimony of James O'Reilly. They argue that while O'Reilly was given immunity from prosecution with respect to his testimony on behalf of the government, he was denied that immunity when called as a defense witness, and therefore that the immunity statutes were applied in a discriminatory manner. This argument is without basis in fact.

After O'Reilly testified for the prosecution, the defense requested that he be excused and recalled pursuant to subpoena. Thus, O'Reilly was available to testify as a defense witness. The only question was whether immunity would be appropriate with regard to matters that might arise on cross-examination. The trial court stated that it would consider the question of immunity "if [O'Reilly] is subpoenaed and any kind of application is made to me" (App. 1472a). However, petitioners did not recall O'Reilly pursuant to subpoena or seek immunity on his behalf. There was in fact no denial of immunity nor any discriminatory application of the immunity statute.

3. Petitioners also urge (Pet. 13-17) that the indictment should be dismissed because they were not given an opportunity to present their defense prior to the time the case was referred by the Intelligence Division of the Internal Revenue Service to the Office of the Regional Counsel. They base their claim upon the Statement of Procedural Rules, Internal Revenue Service, Section 601.107(b)(2) (26 C.F.R., 1972), which provides that "[e]very person who may be the subject of a recommendation for prosecution shall be given an opportunity to explain his participation in the alleged criminal violation prior to the submission of the case to Regional Counsel, unless compelling reasons exist to the contrary." But that provision was de-

leted from the Statement of Procedural Rules effective December 14, 1972, before submission of petitioners' cases to Regional Counsel. See 38 Fed. Reg. 9227. Accordingly, the theory that petitioners advance — that an agency's failure to follow its own regulations is a denial of due process — has no factual application here. Thus, *United States ex rel. Accardi* v. *Shaughnessy,* 347 U.S. 260, upon which petitioners rely, has no bearing on this case. Moreover, a failure by the Intelligence Division to give a taxpayer an opportunity to explain his participation in a criminal violation could not curtail the plenary power of the grand jury to indict. See, *e.g., Sullivan* v. *United States,* 348 U.S. 170, 173; *Lawn* v. *United States,* 355 U.S. 339, 349-350; cf. *United States* v. *Calandra,* 414 U.S. 338, 350.

4. Petitioners' final contention (Pet. 21-23) is that the trial court demeaned their defense and hampered its presentation. Specifically, they complain that the trial court's statement, at an early stage of the trial, that the main factual issue was whether the five payees were fictitious ignored their claim that the amounts had been paid for trucking services rendered. But in their opening statements, defense counsel had not contested the government's assertions that the key factual issue for the jury was whether the five payees in question were real or fictitious, nor did they then discuss the contention, made *inter alia* at trial, that the $145,000 was legitimately expended for trucking services, albeit paid to unidentified persons not listed on the books and records of the corporation. Thus, the trial court's statement was accurate at the time it was made, since no other defense theory had yet been presented. In any event, as petitioners acknowledge, the trial judge accurately set forth their defense in his charge to the jury (Pet. App. 1902a-1903a).

Petitioners also complain that the district court erred in excluding any estimates from Daniel J. O'Connell as to what the cost of removing earth should have been for three of the five job sites. But that ruling was entirely proper. The testimony of O'Connell would not have been based upon facts in evidence (see App. 1612a). It was well within the trial court's discretion to limit O'Connell's estimates and conjectures to those projects, the expenses of which had been put in issue through the introduction into evidence of invoices. *Nelson* v. *Brames,* 241 F.2d 256, 257 (C.A. 10).

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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SUPREME COURT, U. S.

JAN 3 1975

MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-394

MICHAEL PATERNO and PATERNO & SONS, INC.,

Petitioners,

against

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONERS' REPLY BRIEF

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PETITIONERS' REPLY BRIEF

I.

As to the discriminatory application of the Federal immunity statutes.

Contrary to the Government's contention (br., p. 7), the record in this case does squarely present the issue raised in the petition herein (pp. 9-13) as to the propriety of differentiating between the Government and the defense with respect to the availability of the Federal immunity statutes.

The witness James O'Reilly had previously testified for the Government under a grant of immunity. He was thereafter called as a witness by the defense for the purpose of

testifying with respect to certain "technical matters" relating to "the plans, the photographs and the specifications" on the various jobs (1460a).[1] O'Reilly had not been served with any subpoena by the defense, and the limited nature of his anticipated testimony for the defense could not possibly have exposed him to any risk of self-incrimination. O'Reilly's possible need of immunity was suggested only by the prosecutor and the trial court and only in connection with the prosecutor's anticipated cross-examination of O'Reilly (Pet., pp. 10-11).

The trial court first unequivocally announced that the immunity which O'Reilly had received as a Government witness would not extend to any of his testimony as a defense witness (1458a). The court thereafter ruled that it would not grant immunity to O'Reilly as a defense witness because he was appearing voluntarily without having been served with a subpoena by the defense (1467a-1468a). Defense counsel thereupon asked the trial court to allow him to take the time to go to the Clerk's office to obtain a subpoena, but the court refused to do so (1467a-1468a).

The trial court then asked O'Reilly what his position was in view of his possible exposure to the risk of self-incrimination on cross-examination by the prosecutor, and O'Reilly stated, "Maybe I should have immunity again" (1470a). The court also asked O'Reilly whether he would be willing to testify if he did not receive immunity, and O'Reilly stated, "I don't know" (1470a). Defense counsel then acceded to the court's suggestion that the witness be excused until defense counsel could "get a subpoena . . . and consider what . . . [defense counsel] want[ed] to do with him" (1470a).

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[1] Unless otherwise specified, figures in parentheses followed by the letter "a" refer to the pages of defendants' joint Appendix in the Court of Appeals, and "Pet." refers to the petition for certorari herein.

The trial court concluded the matter by stating (1472a):

> "So I will, at Mr. Brill's [defense counsel's] request, excuse Mr. O'Reilly. I do not know how I will proceed if he is subpoenaed and any kind of application is made to me—I simply don't know. * * *
>
> "I must say that if the purposes of calling him are as sharply limited as those described by Mr. Brill I do not see the necessity for going into all this, but if that is the only way it can be done then we will have to face each question as we come to it."

There can be no question that the trial court here flatly ruled that it would not grant O'Reilly immunity with respect to his testimony as a defense witness. The trial court referred to the fact that O'Reilly had not been served with any subpoena by the defense. However, that circumstance was no justification for the court's ruling, since it was only the prosecutor's anticipated cross-examination that occasioned O'Reilly's possible need for immunity, and it was therefore immaterial whether O'Reilly initially took the stand for direct examination pursuant to subpoena or voluntarily.

The rulings made by the trial court, coupled with the intimidating remarks addressed to O'Reilly by the prosecutor and the trial court (see Pet., p. 13), effectually deprived the defense of O'Reilly's testimony as a defense witness. Even though the trial judge's concluding remarks were that he did not know how he would "proceed" if O'Reilly were thereafter subpoenaed and "any kind of application" were made to him, there was no assurance that the trial judge would in any way modify his rulings.

II.

As to the Government's disregard of its published regulations designed for the protection of taxpayers charged with violations of the tax laws.

Contrary to the Government's claim (br., pp. 7-8), the revised regulation here involved, as published in the Federal Register, itself recited that it was first to become effective on April 12, 1973. See Internal Revenue Practice General Procedure Rules, § 601.107(b)(2), amended April 12, 1973, 38 F.R. 9227. The purported change in regulation which, the Government claims, occurred on December 14, 1972, consisted of nothing more than an internal and unpublished memorandum circulated within the Internal Revenue Service ("IRS") on that date. As shown in the petition herein (pp. 15-16), the Government itself admitted in the court below that "the publicly available version" of the above IRS regulation was not "amended to reflect the change" until April 12, 1973.

The Government cites *Sullivan* v. *United States*, 348 U.S. 170, 173, as authority for its position that the Grand Jury had plenary power to indict notwithstanding the Government's violation of its own regulations. The *Sullivan* case, however, is clearly distinguishable. All it involved was an internal letter circulated by the Department of Justice among the various United States Attorneys, and this Court emphasized that that letter "was simply a housekeeping provision of the Department", and that "it was never promulgated as a regulation of the Department and published in the Federal Register" (348 U.S. at 173). In contrast, the present case involves a duly promulgated regulation of the IRS which was published in the Federal Register. The other cases cited by the Government (br., p. 8) are not in point.

III.

As to the false exculpatory statements offered as proof of the essential elements of wilfulness and guilty knowledge.

In an effort to avoid the question raised in the petition herein (pp. 17-21) concerning the effect of the false exculpatory statements made by petitioner Paterno, the Government (br., pp. 3-4, 5-6) has presented an erroneous and misleading version of the evidence. It thus seeks to convey the impression that by virtue of Paterno's being the president and sole stockholder of the corporate petitioner, he must have known that the checks in question were payable to the order of fictitious payees (Govt.'s br., p. 5). It is clear, however, that Paterno's position as president and sole stockholder would not necessarily make him privy to all the details of the manifold operations of the corporate petitioner, particularly the details relating to the arrangements handled by various subordinates for the hiring of trucks on the different construction jobs (see Pet., pp. 5-6), and there was no evidence to show that Paterno in any way participated in, or had any personal knowledge of, such arrangements for the hiring of trucks.

Furthermore, the Government completely ignores the evidence showing that the invoices from the five payees in question were among "hundreds of bills" which would be presented for payment to Paterno at the end of each month; that the company's expenses were very large, amounting to over 11 million dollars during the five-year period here involved; and that the equipment rental expenses alone during that period amounted to $882,808 (see Pet., p. 8).

The Government (br., p. 6, fn. 3) also presents a distorted version of the testimony given by the company's two former bookkeepers. It thus makes no mention at all of the testimony of Mrs. Louise Ferraro, who was the book-

keeper between 1964 and the spring of 1968. Mrs. Ferraro testified that whenever she presented a check to Paterno for signature, she also presented back-up or substantiation material with it, and there was nothing to show that there was any departure from that practice in the case of the checks signed by Paterno to the order of the payees in question during the period of Mrs. Ferraro's tenure (see Pet., p. 7).

As regards the testimony of Mrs. Anne Altro, who was the bookkeeper from May 1968 through 1970, the Government fails to note that her testimony was that whenever she presented a check to Paterno for signature, there were always substantiating delivery tickets attached to the invoices, except on some occasions when co-defendant Denti would instruct her to prepare checks without delivery receipts and would tell her that he would explain the lack of substantiation to Paterno (Pet., pp. 7-8). There was no evidence to show what explanation Denti gave to Paterno on such occasions for the absence of delivery tickets, or to show that Paterno ever signed a check on any such occasion without there being some substantiation therefor, such as entries in the cost sheets (Pet., pp. 20-21).[2]

There are a number of other misstatements in the Government's brief. It thus states (br., p. 6) that after insist-

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[2] There is no support in the record—and none is cited by the Government—for the Government's innuendo (br., p. 6, fn. 3) that petitioners wilfully violated a "subpoena and court order" calling for the production of "delivery receipts from the five payees." There is indeed nothing in the record to show that the prosecutor ever complained about petitioners' failure to produce any delivery receipts pursuant to any subpoena or court order. In fact, the unavailability of delivery receipts was accounted for by the testimony of the bookkeeper Mrs. Ferraro. She thus testified that in the interests of conserving space, her practice was to remove the back-up receipts from the files and dispose of them after some time had elapsed subsequent to the payment of the particular invoices, leaving only the invoices and the cancelled checks in the files (1105a, 1106a, 1120a).

ing that "the five payees were legitimate truckers", both Paterno and Denti "later denied that they had ever heard of the payees." There is however, no support to be found for the latter statement, either in the record references cited by the Government (544a-546a, 628a-630a, 1269a) or elsewhere in the record.

The Government further asserts (br., p. 4) that the witness O'Reilly testified "that he had never heard of the five alleged truckers * * *." However, all that O'Reilly testified to was that *he had no recollection* as to whether any of the five truckers in question had ever worked on one of the Paterno company jobs, and, as a matter of fact, when he was specifically asked with respect to one of the five, Michael Catenzaro, whether he had ever called "a Michael Catenzaro to rent trucks", O'Reilly's answer was: "I might have, I don't know" (1226a).[3]

IV.

As to the action of the trial court in demeaning petitioners' defense and hampering its presentation.

Contrary to the impression sought to be created by the Government (br., p. 8), the trial court's prejudicial statements—to the effect that the basic issue in the case was whether the five payees in question were existent or nonexistent (Pet., p. 22)—were made after defense counsel

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[3] The Government (br., p. 6, fn. 3) also asserts that "there was a staple mark in every one of the invoices from legitimate truckers *in evidence at the trial*" (emphasis supplied). The Government, however, omits to point out that the total number of such invoices introduced in evidence at the trial constituted but a minor fraction of the total Paterno company invoices from "legitimate" truckers. There was clearly not a sufficiently large or representative sampling of such invoices to serve as the basis for the over-all inference sought to be drawn by the Government with respect to all of the Paterno company's invoices from "legitimate" truckers.

had articulated petitioners' defense, that the monies represented by the checks payable to such five payees had actually been expended by the corporate petitioner for the necessary work of hauling away excavated earth from the job sites involved.

As a matter of fact, at the same time that the trial court expressed its views as aforesaid, it also stated in the presence of the jury that any evidence along the lines of petitioners' announced defense, which did not meet the issue as to the existence of the five payees in question, would be excluded as irrelevant (1315a-1317a).

CONCLUSION

For the reasons set forth in the petition herein and in this reply brief, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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